United States Court of Appeals

for the Second Circuit

BRIEF FOR APPELLEE

76-6161

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

No. 76-6161

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff-Appellee,

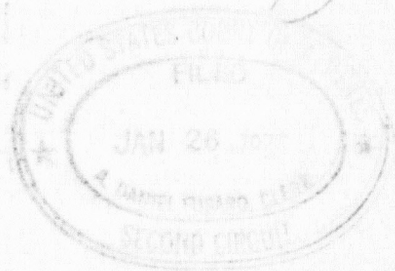
v.

GALAXY FOODS, INC., ARTHUR LIEBERMAN a/k/a ARTY LEE, RALPH AVNI, CHARLES HOROWITZ, BRUCE KATZ, STEVEN ROTH, MARK GLAZER, IRWIN DONALD KIRSCHENBLATT a/k/a DONALD KIRSCH, GEORGE PADILLA, ARTHUR SHEVACK,

Defendants,

IRWIN DONALD KIRSCHENBLATT a/k/a DONALD KIRSCH and ARTHUR SHEVACK,

Defendants-Appellants.



On Appeal from the Judgment of the United States District Court
for the Eastern District of New York

BRIEF OF THE SECURITIES AND EXCHANGE COMMISSION, APPELLEE

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BRIEF OF THE SECURITIES AND EXCHANGE COMMISSION, APPELLEE

COUNTERSTATEMENT OF THE QUESTIONS PRESENTED

1. Did the lower court err in holding that the field manager positions and distributorships in Galaxy were investment contracts for the purposes of the federal securities laws when the purchasers of those interests made substantial investments in Galaxy, which supplied its capital, and were promised a return on their investments that depended upon the efforts of Galaxy's management and the success of the Galaxy enterprise and that required no significant efforts by the investors themselves?

2. Did the lower court err in holding that Kirsch and Shevack violated Section 10(b) of the Exchange Act by knowingly or recklessly misrepresenting and omitting to state material facts in connection with the offer and sale of investment contracts in the form of interests in Galaxy?

COUNTERSTATEMENT OF THE CASE

A. Nature of the Case and Proceedings Below

This is an appeal by Irwin Donald Kirschenblatt, a/k/a Donald Kirsch, and Arthur Shevack, from an order (A 1826-30)[1/] entered on September 13, 1976, by the United States District Court for the Eastern District of New York, permanently enjoining them from engaging, directly or indirectly, in violations of the registration[2/] and antifraud provisions[3/] of the federal securities laws. The district court found that Kirsch and Shevack had violated and aided and abetted violations of those provisions in connection with the offer and sale of investment contracts in the form of distributorship interests and field manager interests in Galaxy Foods, Inc., and that, unless enjoined, Kirsch's and Shevack's violative conduct was likely to continue in connection with their current business activities (A 1809-13). The court also directed Messrs. Kirsch and Shevack to disgorge profits obtained from their unlawful activities in the amount of $3,700 plus interest and $8,250 plus interest, respectively (A 1830).

The Commission's complaint, filed November 26, 1973, alleged that Kirsch and Shevack, together with Galaxy Foods, Inc., Arthur Lieberman,

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1/ Pages in the Joint Appendix are cited as "A __."

2/ Section 5 of the Securities Act of 1933, 15 U.S.C. 77e.

3/ Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a), and Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b), and Rule 10b-5 thereunder, 17 CFR 240.10b-5.

a/k/a Arty Lee, Ralph Avni, Charles Horowitz, Bruce Katz, Steve Roth, Mark Glazer and George Padilla, had violated and were about to violate Sections 5 and 17(a) of the Securities Act of 1933 ("Securities Act") and Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 10b-5 thereunder, in connection with offers to sell and sales of interests in a pyramid promotional scheme operated by Galaxy.[4/] The complaint sought a permanent injunction against future violations of these provisions of the federal securities laws and disgorgement of the illicit profits received by the defendants. (A 3a-27a.) All the individual defendants, except appellants, have consented to the entry of judgments against them, which included permanent injunctions and directions to disgorge unlawfully-obtained profits (A 1757-58).[5/]

B. Facts

1. The Galaxy Scheme

Galaxy Foods, Inc. (hereinafter "Galaxy"), was incorporated in New York State in September 1971, for the purported purpose of buying and distributing food, and other items available in supermarkets, and for the purpose of offering and selling "sales distributorships" (A 1758, 1954-56).

Galaxy claimed to have "devised a remarkable new way of reaching and servicing" the consumer of supermarket items, through "a phone order, home

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4/ The interests offered and sold were alleged to be securities as defined by Section 2(1) of the Securities Act, 15 U.S.C. 77b(1), and Section 3(a)(10) of the Exchange Act, 15 U.S.C. 78c(a)(10) (A 3a-27a).

5/ Consent decrees were entered against Arthur Lieberman, a/k/a Arty Lee, Ralph Avni, Charles Horowitz, Bruce Katz, Steve Roth, and Mark Glazer prior to trial. During the trial, which lasted eight days, defendant Padilla consented to the entry of a similar judgment. (A 1757-58.) Prior to the trial, on November 28, 1973, Galaxy Foods, Inc., filed a voluntary petition in bankruptcy and this action was stayed as to it (A 1774).

delivery service," whereby consumers would be able to select name brand items from a catalogue, order them by phone and have them delivered to their homes, without a delivery charge, at prices "highly competitive" (emphasis in original) with those of supermarkets (A 1835). As described by Galaxy, the proposed sale of groceries would be generated by a three-tier sales force consisting of salespersons, field managers and distributors, with the "distributors" occupying the "highest position" (A 1841-42). The salespersons were to do the actual selling; and Galaxy claimed field managers and distributors could "earn large sums of money merely by recruiting salesmen and having them introduce our service to consumers" (A 1836).

In the Galaxy hierarchy, a distributor was to have both field managers and their salespersons in his "organization" (as well as any salespersons he himself recruited), and was to receive commissions on their sales. A field manager, the lower of the two positions, was to earn commissions only on sales by his salespersons and on his own sales. Field managers were promised a five percent override commission on initial orders by new customers recruited by their salespersons and a two percent override commission on their reorders; as well as a ten percent commission on the initial orders of all new customers they obtained themselves and a three percent commission on reorders. A distributor was promised a five percent commission on initial orders generated by field managers he had sponsored (introduced to Galaxy) or their salespersons and a two percent override commission on reorders. Distributors also were promised a 15 percent commission on the initial orders of customers they brought to Galaxy and a five percent commission on their reorders. Salesmen were to receive a five percent commission on initial orders and a one percent commission on reorders. (A 1839-42, 1844, 1847-49.) Considering these commissions, it is

difficult to perceive how Galaxy would be able to charge prices that would be "highly competitive" with the prices in supermarkets (emphasis in original; A 1835).

But, Galaxy's retail operations, unlike its sales of distributorships and field manager positions, never effectively began (A 1773). Although Galaxy did initiate a retail sales "pilot program," that program lasted only four months,[6/] and gross sales totalled a mere $160,814.[7/] On the other hand, from the sale of some 800 distributorships and field manager interests Galaxy raised more than $2.4 million from its earliest sales in September 1971 until Galaxy's bankruptcy in November 1973. (A 280-81, 1773-74.) In contrast, the founders of Galaxy--Lieberman, Avni and Rosenthal--contributed only a total of $100 to Galaxy's capital (A 1997-2000, 2006). Indeed, Mr. Lieberman—an incorporator, stockholder, and the chairman of the board of Galaxy (A 264, 272, 1816, 1864)--testified that the capital necessary for Galaxy's operations was to be raised from the sale of the distributorships and field manager positions (A 265, 280).

Galaxy referred to the field manager positions and distributorships, discussed above, as investments (A 281, 1841-1843, 1847-48, 1856, 1873, 1888-89). A field manager position initially sold for $1,000; however, the price was increased to $2,000 in March 1972, and to $3,000 in October 1972. Distributorships initially sold for $3,000, but were increased to $5,000 in March 1972 and to $7,000 in October of that year. (A 281, 1759.) In addition to the promised commissions on retail sales by salespersons, the purchasers of field manager

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6/ While Galaxy paid a few commissions in connection with this program in March 1973, in response to vigorous protesting by its investors, these were the only commissions paid on retail sales during its existence (A 1773).

7/ Sales during the pilot program totaled $160,814; the cost of the goods purchased for the program was $201,630 (A 1773, 2003), resulting in a net loss. The program began on November 27, 1972, and was terminated on March 31, 1973 (A 1773).

and distributor positions were promised, and in fact received, commissions for "bringing in" (A 280) new investors as field managers or distributors. Distributors, presumably in recognition of their higher investments, received a larger payment. After October 1972, when field managers were required to invest $3,000 and distributors $7,000, field managers received $750 for sponsoring new field managers or distributors in Galaxy and distributors received $1,050 for sponsoring new field managers and $2,450 for sponsoring new distributors. Distributors also received $350 if a field manager they sponsored brought a new field manager into the Galaxy operation, plus $1,400 more if that new field manager later became a distributor. (A 1760-61, 1842-43, 1847-49.)

A chart prepared by Galaxy titled "WHAT IS THE BEST WAY FOR YOU TO PUT YOUR MONEY TO WORK FOR YOU" contrasted, as a "type of investment," a $5,000 Galaxy distributorship with a $5,000 "investment" in a savings bank, securities or real estate, and asserted that the interest in Galaxy would give the best "RETURN ON YOUR INVESTMENT" (A 1873). No registration statement covering these interests in Galaxy was ever filed with the Commission (A 1832).

2. Sales of Investments in Galaxy

Galaxy sold its field manager positions and distributorships, which the district court held to be "investment contracts" (A 1791-92), at promotional meetings of two types, "opportunity meetings" and "Sunday step-up meetings." Opportunity meetings were held three or four times a week at various hotels in and near New York City; step-up meetings were held at Galaxy's business office or its rented warehouse in Brooklyn every Sunday, but one, while Galaxy was in business. (A 297-98, 1761-64.). In addition, Galaxy regularly conducted training sessions for its field managers and distributors where they were trained in the techniques of "prospecting" or inducing

others to attend opportunity meetings. One method, called "cold canvassing," involved approaching strangers on the street, and elsewhere, and attempting to persuade them to attend a meeting by asking "would you like to have an opportunity to see a business where you could earn perhaps what you are worth rather than what somebody else thinks you are worth." (A 336-37,342, 356-57, 361-62, 366-67, 1764-65.) Practice exercises were held at these training sessions, and "Dare To Be Great" tapes were played (A 1765).[8/]

Galaxy distributors and managers were told to invite prospects to opportunity meetings, but to give them little, if any, information about Galaxy itself. Prospects were to be lured by the possibility of earning large sums of money. Distributors and managers were to drive new, expensive automobiles, wear expensive clothes and carry large sums of cash to give prospects the impression that their investments in Galaxy were extremely profitable. (A 365-66, 371, 1762-63.)

The speakers at the opportunity meetings, other than the "guest speaker" (usually a top Galaxy official), were not allowed to deviate from a script prepared by Galaxy. Speakers would explain the commissions paid investors and, using a blackboard, diagram how an investor purportedly could earn as much as $60,000 per year within three months after investing in Galaxy. The guest speaker would promise that Galaxy would, itself, distribute 8,000 to 10,000 customers among its distributors and field managers when retail operations began. (A 305-11, 1761-62, 1834-44.)

8/ Dare To Be Great was a subsidiary of Glenn W. Turner Enterprises, Inc. See Securities and Exchange Commission v. Glenn W. Turner Enterprises, Inc., 474 F. 2d 476 (C.A. 9), certiorari denied, 414 U.S. 821 (1973).

The script used by speakers at the opportunity meetings began:

> "Good evening, ladies and gentlemen. Tonight we would like to present an idea to you--an idea which could revolutionize the food industry and could conceivably make you financially successful beyond your grandest dreams. Keep in mind that what you are about to see tonight is a proven vehicle for success and the marketing plan we will be discussing has been used successfully to make men and women thousands and even millions of dollars.
>
> * * *
>
> "It is my responsibility . . . to explain how you can earn large sums of money merely by recruiting salesmen and having them introduce our service to consumers." (Emphasis in original; A 1835-36.)

Speakers represented that if an investor in Galaxy recruited just two salesmen, who achieved a certain stated level of orders and reorders in their first month, that investor could earn $10,000 per year without recruiting any additional salesmen and without any additional sales by the two salesmen (A 1839-40). They further represented that if the investor recruited two more salesmen in the second month and two more the third month, and these salesmen, each, in one month achieved the same sales level, the investor, without further efforts by existing salesmen, "could earn $60,000 per year," from commissions on the telephone "reorders" placed directly with Galaxy by the customers their salesmen previously contacted (A 1840-41).

At the opportunity meetings, investors were promised that salesmen would be trained, their customers would be given a local telephone number to call, the customers' telephone orders would be taken by Galaxy and delivered in its own trucks from its warehouse without charge. The salesmen would not be required to reservice or recontact their customers, who would order from the Galaxy catalog; and, as indicated above, the salesmen, and the investors

who recruited them, were promised commissions from Galaxy on any subsequent orders by the customers. (A 1771-1772, 1836-42.)

Potential investors who succumbed during an opportunity meeting and agreed to invest were called to the front of the room and their names and the interests they had agreed to purchase were announced (A 320-21).

Prospects who did not succumb were invited to a Sunday step-up meeting, a meeting designed to "close the sale" (A 297). This was referred to as "GTC" --getting the check--by Galaxy (A 383, 1763). Galaxy's management intentionally created a high-pressure atmosphere at these meetings to imbue the prospects with an almost irrational desire to invest in Galaxy (A 1764). They told existing investors to sit next to the prospects they brought to the meetings, to applaud the speakers and generally to exhibit great enthusiasm (A 1765). Lieberman referred to this as "jack-up" (A 1764).[9/] A top Galaxy official would give a speech stressing the amount of money which could be received by investors in Galaxy (A 322, 920).

Another feature of these "Sunday step-up meetings," called "pay-day," involved handing out commission checks to managers and distributors, and announcing the amounts involved, amidst loud applause and cheering (A 330-32, 1763-64). Near the end of the meeting, prospective investors were called to the front of the room, asked their name, etc., and whether they were going to "join" as a field manager or distributor. Affirmative responses were greeted with more applause and cheering. (A 322-24, 1127-28, 1764.)

9/ Howard Beck, an investor introduced to Galaxy by Kirsch, testified that Lieberman had explained that "jack-up" "means to get someone thoroughly involved in the idea that they are so enthusiastic about it that they forget everything." (A 917.)

Galaxy told managers and distributors to suggest ways interested prospects could raise funds needed to invest in Galaxy. They were to inquire whether the prospect had insurance policies with cash values, to suggest getting a loan from a bank or finance company and to find out if the prospect had money in a savings account which could be borrowed against. They were to drive the prospect to a lending institution if he were to try to get a loan and to tell him to put down the purchase of furniture as the reason for the loan. (A 383-84, 1765.)

Galaxy's organization, including its "commission" structure and promotional efforts, especially the opportunity meetings, were patterned after Koscot Interplanetary, Inc.[10/] The founders of Galaxy had formerly been associated with Koscot, as had both Kirsch and Shevack, who met Lieberman, Galaxy's chairman, when all three men had been associated with Koscot. (A 1767, 1775, 1781.)

3. Kirsch's Participation in the Galaxy Scheme

Kirsch joined Galaxy in August 1971, and continued with Galaxy until he resigned in early 1973, after expressing dissatisfaction with his superiors in Galaxy's management (A 1774, 1945-46). He held the position of executive vice-president in charge of marketing and was one of eight members of Galaxy's "executive board" (A 1775),[11/] which met weekly to discuss events of the previous week and made decisions regarding the location, frequency and identity

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10/ See, Securities and Exchange Commission v. Koscot Interplanetary, Inc., 497 F. 2d 473 (C.A. 5, 1974).

11/ The board of directors, a separate body from the executive board, established policy and could veto any action of the executive board (A 1766-67).

of speakers at the "opportunity" meetings. The executive board also discussed the advisability of cheering and applauding at meetings, the practice of handing out checks at the "Sunday step-up" meetings and other issues related to the content, purpose and format of the meetings. (A 316-17, 328-34, 1766-67.) Among other things, Kirsch attended the meeting at which the executive board approved the newspaper advertisements used by Galaxy (A 1775) which stated: "ARE YOU READY TO EARN $50,000 PER YEAR" and referred to a "guaranteed investment" (A 1856, 1888-89).

Kirsch attended at least 50 to 75 "opportunity" meetings and spoke at least once a month at these meetings. He attended 25 to 35 "Sunday step-up" meetings and assisted in selling field manager positions and distributorships to prospective investors during and after the presentations at the "opportunity" and "step-up" meetings. (A 1776.) Like other Galaxy executives, Kirsch received an override commision of 1/2 to 1% of total franchise sales as a "salary" (A 1776).

Kirsch also personally recruited three individuals who invested in Galaxy (A 1775). One investor, Howard Beck, a salesman at E. J. Korvette (A 882), testified that he was driving through the Queens Midtown Tunnel when he was handed a flyer from a passing car driven by Kirsch. The flyer had Kirsch's name and telephone number on it and asked: "Would you like to earn over $2,000 per month? Would you like to double this figure within the following 12 months? Would you like the idea of being closely associatd with a man who at the age of 35 is a multi-millionaire and who will teach you his techniques for accumulating wealth and success? Would you like to be financially able to vacation at least 2 months out of every year . . .?" (A 1776-77, 1900.)

Beck telephoned Kirsch and was invited to a Galaxy meeting. After attending that and a subsequent meeting, he told Kirsch he would invest $1,000 to purchase a field manager position. When Beck met Kirsch to sign an application and deliver the $1,000, however, he discovered that Kirsch had filled out an application for a distributorship, a $3,000 investment. Beck told Kirsch he did not have $3,000, so Kirsch suggested that he get a bank loan and said Beck could use Kirsch's corporation—K Enterprises, the name of his former Koscot distributorship—as a credit reference. Kirsch also instructed Beck to tell the bank the loan was for furniture. (A 197, 1777-78.)

Kirsch drove Beck to a bank and accompanied him when he spoke with a bank officer. When the bank did not make the loan, Kirsch suggested trying another bank, but Beck refused. Kirsch then crossed out "distributor" and "$3,000," substituted "manager" and "$1,000" on the application. (1778-79, 1902.) 12/

After investing in Galaxy, Beck adopted Kirsch's flyer 13/ for his own use by substituting his name and phone number for Kirsch's (A 909-10, 938, 1780). Accompanied by Kirsch, Beck went to different areas of New York and passed out his and Kirsch's flyers. He observed Kirsch approach people and attempt to persuade them to attend a Galaxy meeting. (A 909-10.)

12/ The court noted that Kirsch's testimony regarding this attempt to secure a loan for Beck contradicted Beck's version of the same event. The court found, however, that Kirsch's "trial testimony concerning that loan episode is contradicted by his previous testimoney before the SEC where he admitted suggesting that Beck take out a loan." (A 1779.)

13/ Kirsch later told Beck the flyer had applied to another business (and the court presumed this to be Koscot) (A 940-41, 1780, 1806). See n. 10, supra.

Kirsch testified that he explained to Beck, and the other two individuals he recruited, that they should approach people, including strangers, and ask if they were interested in becoming part of a company "that could possibly earn them a good amount of money" (A 63). He told them to say nothing about Galaxy itself, but simply try to get the person to come to a meeting (A 64-5).

4. Shevack's Participation in the Galaxy Scheme

In June 1972, Shevack met Lieberman, whom he had known when they both were associated with Koscot, at a catering hall, and Lieberman invited him to an opportunity meeting which Galaxy was holding there, telling Shevack that Galaxy "fits you like a glove" (A 1471, 1781). After the meeting, Lieberman told Shevack, who said he did not have the $5,000 needed to purchase a distributorship, that he could "work his way into the business" by recruiting others (A 1473-74, 1781). Within the next two months, Shevack had recruited five or six individuals who invested in Galaxy and, with the $5,000 in commissions he received, purchased a distributorship for himself (A 1781). From July 1972, until he sold his distributorship in approximately December 1972, for $5,500, he recruited approximately 10 additional investors in Galaxy and received over $11,000 in commissions on these sales (A 1485, 1782).[14/]

Shevack had hundreds of cards printed, which he handed out when he was "cold canvassing". The cards asked, "[A]re you ready to earn $50,000 per year" and referred to "a $2,000 or $5,000 if not totally satisfied guaranteed money back investment." (A 1782.)

14/ Shevack testified that he split these commissions with a partner (A 1486).

Melvin J. McLean, then a bank securities clerk earning $140 per week, was approached by Shevack, whom he had never met, while he was on a lunch break (A 1208-9, 1784). Shevack asked McLean, "How would you like to earn about $50,000 a year", and invited him to attend an "opportunity" meeting that night, refusing to answer McLean's questions and saying he was "in a hurry" (A 1208, 1784). McLean attended the meeting and Shevack drove him home (A 1218-19). During the ride, Shevack told McLean that before he joined Galaxy he was making $125 per week working on Wall Street, that since joining Galaxy (earlier that summer) he had already made $30,000 to $40,000, that he had bought a new Cadillac Eldorado and that he was buying a new home (A 1219-20, 1784).

McLean indicated he did not have the funds necessary to invest and Shevack told him he himself had borrowed the money needed and could help McLean get money if he really wanted to join (A 1219, 1784). A few days later Shevack called McLean and told him they could try to get him a loan from a bank. When McLean said he already owed money, Shevack told him not to worry because he would be able to pay off the loan (A 1221, 1784). McLean finally succumbed to Shevack's urgings (A 1221-22, 1785).

Shevack met McLean at a bank and told him to put on the loan application that the loan was for furniture and that his wife was working for a company in Brooklyn. When McLean objected that this was not true, Shevack said that if the bank called the company, they would be told his wife worked there. The loan was not approved. (A 1222-27.) Shevack subsequently took McLean to Household Finance where McLean borrowed $700. Shevack took the $700 and said McLean could earn the additional money needed by recruiting others. (A 1226-31, 1233, 1785.)

Branch Simmons and Steven Silverman were recruited by Shevack in a generally similar fashion (A 1109-11, 1141-46, 1304-07, 1319-28, 1344, 1782-83, 1785-87). For example, Shevack gave Silverman a false W-2 form for Mrs. Silverman, who was unemployed, and a telephone number to be called should further verification that his wife was working be needed by the bank from which Silverman was to seek a loan (A 1322-24, 1786). Although Shevack denied having given Silverman the false W-2 form, and denied driving McLean to a bank or otherwise assisting McLean or Simmons to borrow money (A 1504-05, 1507-14), the court found:

> "The similarity of Shevack's modus operandi as described by McLean, Simmons, and the Silvermans coupled with the fact that this was the same method taught at the Galaxy training sessions attended by Shevack, leads inexorably to the conclusion that he did suggest borrowing to these people, that he did drive them to the lending institutions and that he did induce them to give false answers on the loan applications." (A 1787.)

5. Kirsch and Shevack's Current Activities

Since 1973, Kirsch and Shevack have been associated with Futuristic Foods, which was purportedly formed to provide "a phone-order, home delivery service for all supermarket items" (A 1810, 1939). Shevack, one of Futuristic's three incorporators, admitted he copied the Futuristic operations from Galaxy. And, like Galaxy, Futuristic sold two different investment interests to gain working capital, a "silver" franchise which originally sold for $3,000 and a "gold" franchise which originally sold for $6,000. Purchasers of these interests were promised commissions on retail food sales by Futuristic and on sales of investments to persons they sponsored. (A 175-76, 1631-32, 1810.)

On August 23, 1974, about nine months after the instant action was filed, the Commission filed an action in the United States District Court for the Southern District of New York seeking to enjoin alleged violations of the registration and antifraud provisions of the federal securities laws by Futuristic Foods, Kirsch, Shevack and other named defendants. See Securities and Exchange Commission v. Futuristic Foods, Inc., et al., 74 Civ. 3665 (WCC) (S.D. N.Y.). On June 18, 1976, the district court entered a permanent injunction by consent against certain of the defendants in that case, including Kirsch and Shevack.

C. The District Court's Decision

Based on its findings of fact (A 1758-88), the district court in the instant case concluded that the Galaxy "franchises" (field manager positions and distributorships) were investment contracts within the meaning of Section 2(1) of the Securities Act and Section 3(a)(10) of the Exchange Act (A 1792), and were subject to the registration requirements and antifraud provisions of those Acts (A 1796, 1800). The court further found that no registration statement covering these securities had ever been filed and no exemption from the registration requirements was available (A 1796-99). Finally, the court found that, in connection with the offer and sale of these securities, Kirsch and Shevack had aided and abetted violations by Galaxy of Section 5 and violated and aided and abetted violations of Sections 17(a) of the Securities Act and 10(b) of the Exchange Act and Rule 10b-5 thereunder (A 1799-1800, 1805-08).

With respect to the alleged fraud violations, the court held:

> "it seems clear that the totality of the carnival-type Opportunity and Step-Up Meetings, the 'Jack-Up' objective and the 'fake it 'til you make it' approach to selling constitutes a

> manipulative and deceptive device proscribed by §17(a)(1) and (3) of the Securities Act, §10(b) of the Exchange Act and Rule 10b-5(1) and (3). The psychological selling techniques employed by Galaxy successfully duped many innocent, though unwise, investors into parting with funds, often borrowed, which they could ill-afford to invest even in far safer enterprises." (A 1800.)
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> * * *
>
> "It would take pages to list all the untruths, half-truths and unrealistic projections and predictions contained in the presentations and literature associated with Galaxy." (A 1802.)

Specifically with respect to Kirsch, the court found that he participated in the "overall fraudulent scheme" and that "he was surely aware of the many misrepresentations and omissions and the unsavory nature of the fraudulent high-pressure selling being employed" (A 1805-06). In addition to finding that Kirsch aided and abetted Galaxy's fraud violations through "[h]is involvement in the entire Galaxy operation," and by causing the three investors he sponsored "to be exposed to Galaxy's fraudulent conduct," the court found that he was primarily responsible for antifraud violations committed in the course of recruiting Beck. Among other things, the court found that Kirsch had recruited Beck using a flyer containing patently false statements which, in view of Kirsch's familiarity with Galaxy and his knowledge that the flyer had been prepared in connection with another business, Kirsch either knew were false or made with reckless disregard for their truth or falsity. (A 1805-86.)

With respect to Shevack, the court found that, like Kirsch, he had aided and abetted Galaxy's violations by recruiting investors and causing them to be exposed to the "Galaxy 'sell-machine'" and by participating in at least one training session (A 1807). Moreover, the court found that his "prospecting

and sponsoring activities, which can best be characterized as unscrupulous, are more than sufficient to establish primary liability for antifraud violations" (A 1807-08). The court found that among his "more blatant material false statements" were representations that he had already earned $30,000 to $40,000 from Galaxy, that he had purchased a new Cadillac from his earnings and that the investments were completely guaranteed. The court also found that Shevack's "misrepresentations were uttered either knowingly or with reckless disregard for their truth or falsity." (A 1807-08.)

The court concluded that, in light of Kirsch and Shevack's violations of the registration requirements and their knowing and reckless violations of the antifraud provisions of the federal securities laws in connection with the purchases and sales of Galaxy "franchises," as well as their subsequent involvement in similar activities through their association with Futuristic Foods, the relief sought by the Commission--permanent injunctions against future violations and disgorgement of unlawfully obtained profits--was appropriate. (A 1809-15.)

ARGUMENT

THE DISTRICT COURT PROPERLY FOUND THAT APPELLANTS OFFERED AND SOLD SECURITIES IN VIOLATION OF THE REGISTRATION AND ANTIFRAUD PROVISIONS OF THE FEDERAL SECURITIES LAWS.

A. The Interests in Galaxy Offered and Sold by Appellants Were Securities.

The jurisdictional challenge raised by appellants (Br. 11-15) turns on whether the interests in Galaxy they offered and sold are securities within the meaning of Section 2(1) of the Securities Act and Section 3(a)(10) of the Exchange Act.[15/] This issue has already been determined by the

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15/ The broad definitions of security set forth in those sections, are, so far as here involved, substantially identical and should be read in pari materia (see Tcherepnin v. Knight, 389 U.S. 332, 335-336 (1967)). They include a "certificate of interest or participation in any profit sharing agreement," an "investment contract" and "in general, any interest or instrument commonly known as a security.'"

Specifically, Section 2(1) of the Securities Act, 15 U.S.C. 77b(1), provides:

> "The term 'security' means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas or other mineral rights, or, in general, any interest or instrument commonly known as a 'security,' or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing."

Section 3(a)(10) of the Exchange Act, 15 U.S.C. 78c(a)(10), similarly provides:

> "The term 'security' means any note, stock, treasury stock, bond, debenture, certificate of interest or participation in any profit-sharing agreement or in any oil, gas or other mineral royalty or lease, any collateral-trust certificate, preorganization certificate or subscription, transferable

(continued)

United States Courts of Appeals for the Fifth and Ninth Circuits in Securities and Exchange Commission v. Koscot Interplanetary, Inc., 497 F. 2d 473 (C.A. 5, 1974); and Securities and Exchange Commission v. Glenn W. Turner Enterprises, Inc., 474 F. 2d 476 (C.A. 9), certiorari denied, 414 U.S. 821 (1973), respectively; cases in which schemes with commission structures and promotional techniques substantially identical to those of Galaxy were held to involve the offer and sale of investment contracts. 16/

The test applied by both the Courts of Appeals for the Fifth and Ninth Circuits, in the cases cited above, to determine the existence of an investment contract, 17/ which was adopted and applied by the court below (A 1789-90), is consistent with the past interpretation of "investment

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15/ (continued)

> share, investment contract, voting-trust certificate, certificate of deposit, for a security, or in general, any instrument commonly known as a 'security'; or any certificate of interest or participation in, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing; but shall not include currency or any note, draft, bill of exchange, or banker's acceptance which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited."

16/ The court below found that the "organizational arrangement and promotional nature of Galaxy--particularly the concept of non-exclusive franchisees, the Opportunity Meetings and the commission structure--was patterned in large part after that employed by a company called Koscot Interplanetary, Inc." (A 1767), the defendant in the Fifth Circuit case cited above; Koscot itself was a "promotional scheme . . . largely paralleled" by the scheme considered by the Ninth Circuit in Glenn W. Turner, supra. Koscot Interplanetary, Inc., supra, 497 F. 2d at 484.

17/ "[W]hether the efforts made by those other than the investor are the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise." Koscot Interplanetary, Inc., supra, 497 F. 2d at 483, quoting from Glenn W. Turner Enterprises, Inc., supra, 474 F. 2d at 482.

contract." See, Securities and Exchange Commission v. United Benefit Life Insurance Co., 387 U.S. 202 (1967); Tcherepnin v. Knight, 389 U.S. 332 (1967); Securities and Exchange Commission v. Variable Annuity Life Insurance Co., 359 U.S. 65 (1959); Securities and Exchange Commission v. W. J. Howey Co., 328 U.S. 293 (1946); Securities and Exchange Commission v. C. M. Joiner Leasing Corp., 320 U.S. 344 (1943). The recent Supreme Court decision in United Housing Foundation Inc. v. Forman, 421 U.S. 837 (1975), in no way repudiated these decisions.[18/]

Remedial legislation, such as the federal securities laws, must be construed "not technically and restrictively, but flexibly to effectuate [its] remedial purposes," Affiliated Ute Citizens v. United States, 406 U.S. 128, 151 (1972). This basic canon of statutory construction is applicable to the definitions of security set forth in those Acts. See Tcherepnin v. Knight, supra, 389 U.S. at 336.

As the Supreme Court held in Securities and Exchange Commission v. W. J. Howey Co., supra, 328 U.S. at 299, where orange groves with service contracts were held to be "investment contract[s]," the statutory definition of a security

> "embodies a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of money of others on the promise of profits.
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> * * *
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> "The statutory policy of affording broad protection to investors is not to be thwarted by unrealistic and irrelevant formulae." Id. at 301.

In determining the existence of a security, therefore, "form should be

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18/ See n. 22, infra.

disregarded for substance and the emphasis should be on economic reality." Tcherepnin v. Knight, supra, 389 U.S. at 336; Securities and Exchange Commission v. W. J. Howey Co., supra, 328 U.S. at 298.

> "The test rather is what character the instrument is given in commerce by the terms of the offer, the plan of distribution and the economic inducements held out to the prospect. "

Securities and Exchange Commission v. C. M. Joiner Leasing Corp., supra, 320 U.S. at 352-53. 19/

19/ The legislative history of the Securities Act shows that it was adopted:

> ". . . to prevent further exploitation of the public by the sale of unsound, fraudulent, and worthless securities through misrepresentation before the investor; to protect honest enterprise, seeking capital by honest presentations, against the competition afforded by dishonest securities offered to the public through crooked promotion; . . . ." S. Rep. No. 47, 73d Cong., 1st Sess. 1 (1933).

A principal purpose of that Act was to assure that "persons . . . who sponsor the investment of other people's money should be held up to the high standards of trusteeship, in contrast to what occurred in the decade after the First World War:

> ". . . $25,000,000,000 worth of securities floated . . . proved to be worthless. These cold figures spell tragedy in the lives of thousands of individuals who invested their life savings, accumulated after years of effort, in these worthless securities . . . alluring promises of easy wealth were freely made with little or no attempt to bring to the investor's attention those facts essential to estimating the worth of any security. High-pressure salesmanship rather than careful counsel was the rule in this most dangerous of enterprises." H.R. Rep. No. 85, 73d Cong., 1st Sess. (1933) at 2-3.

In an attempt to ensure that this legislative purpose would be accomplished, "security" was defined in the Securities Act

> "in sufficiently broad and general terms so as to include . . . the many types of instruments that in our commercial world fall within the ordinary concept of a security," H. R. Rep. No. 85, supra, at 11.

(continued)

The first case in which the Supreme Court considered the breadth of the application of the federal securities laws and the scope of the term "investment contract" was Securities and Exchange Commission v. C. M. Joiner Leasing Corp., supra. The lower courts had found that the interests sold by the defendants in that case were not securities, holding that there had been "simply sales and assignments of legal and legitimate oil and gas leases, i.e., sales of interests in land." 320 U.S. at 348. In this regard, the lower courts' holdings in Joiner are similar to the arguments advanced by Kirsch and Shevack that the interests in Galaxy were simply franchises, not investment contracts. In Joiner, however, the Supreme Court squarely rejected this argument, holding that the defendants had not simply offered purchasers a naked lease "[leaving] them to their own devices for realizing upon their rights," but

> "a chance, without undue delay or additional cost, of sharing in discovery values which might follow a current exploration enterprise.
>
> * * *
>
> "The exploration enterprise was woven into these leaseholds, in both an economic and a legal sense; the undertaking to drill a well runs through the whole transaction as the thread on which everybody's beads were strung." 320 U.S. at 348 (emphasis supplied).

Similarly, Galaxy promised prospective investors commissions on the sale of distributorships and field manager positions which depended, in

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19/ (Footnote continued)

The concerns underlying the Exchange Act and its intended scope were similar. It was enacted in response to "the speculative orgy of 1928 and 1929," see, S. Rep. No. 1455, 73d Cong., 2d Sess. 81 (1934), and was intended to cover "a wide field." H. R. Rep. No. 1383, 73d Cong., 2d Sess. 5 (1934).

fact, upon the success of the Galaxy enterprise. As the district court below concluded:

> "[P]rospective franchisees [purchasers of distributorships or field manager positions] were being asked to invest substantial sums of money in Galaxy . . . simply [for] the opportunity to earn money if the efforts of others, Galaxy's management and the salespeople, proved successful." (A 1794-95.)

In short, the investor was, in the common sense, investing in Galaxy, and the success of the enterprise was the "thread on which everybody's beads were strung" (320 U.S. at 348). Therefore, these interests in Galaxy were investment contracts.

Appellants Kirsch and Shevack nevertheless argue that these interests in Galaxy were not investment contracts (Br. 11-15), stressing the Supreme Court's statement in Securities and Exchange Commission v. W. J. Howey Co., supra:

> "The test [of an investment contract] is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others." 328 U.S. at 301. (Emphasis supplied.)

Focusing on the word "solely" in the above-quoted language, appellants contend (Br. 11-12) that the limited efforts required of investors in interests in Galaxy foreclose a finding that these interests were investment contracts. But, as the Court of Appeals for the Ninth Circuit stated in Glenn W. Turner Enterprises, Inc., supra, 474 F. 2d at 482, if this narrow, unrealistic definition of investment contract were adopted,

> "[i]t would be easy to evade by adding a requirement that the buyer contribute a modicum of effort. Thus the fact that the investors here were required to exert some efforts . . . should not automatically preclude a finding that the . . . [interest in question] is an investment contract. To do so would not serve the purpose of the legislation."

Thus, the court in Turner applied the following test to determine the existence of an investment contract:

> "whether the efforts made by those other than the investor are the undeniably significant ones, those essential management efforts which affect the failure or success of the enterprise." Id.

Accord, Securities and Exchange Commission v. Koscot Interplanetary Inc., supra, 499 F. 2d at 483. 20/

Applying that test to the facts in the instant case, Galaxy's distributorships and field manager positions clearly qualify as investment contracts. As discussed above, the efforts to be expended by investors to receive commissions on the sale of its distributorships were not the "undeniably significant ones." Galaxy took the primary laboring oar for "Getting the Check" from prospective investors, thereby providing a return on the investors' capital.

Appellants argue (Br. 15-16) that the distributorships and field manager positions in Galaxy should not be considered securities because the commissions paid distributors and field managers on the sale of similar

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20/ Defendants argue (Br. 14-15) that the Commission itself has adopted the test set forth in State v. Hawaii Market Center, Inc., 485 P. 2d 105 (Ha. 1971), for determining whether a franchise is an investment contract, and that, applying that test to the facts in this case, this Court should find that the distributorships and field manager positions offered and sold by Galaxy were not securities. See Securities Exchange Act Release No. 9387 (November 30, 1971).

Defendants err in two respects. First, they misread the test adopted in Hawaii Market Center. The Supreme Court of Hawaii did not hold, as appellants assert, that, in order for an investment contract to exist, "the franchisee would have to be controlled by corporate management" (Br. 14); rather, the court held that

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interests to others were a "gratuitous privilege" not a contractual right. Appellants' argument is without substance. As a practical matter, those commissions were the only way to make money in Galaxy (A 1791). Compare Joiner, discussed at page 23, supra, where the Supreme Court held that assignments of oil and gas leases were investment contracts since, as a "practical matter", the sale included representations that exploratory wells would be drilled. The Supreme Court analyzed the substance of the transactions and stated:

> "Whether . . . the assignee acquired a legal right to compel the drilling of the test well is a question of state law which we find it unnecessary to determine." 320 U.S. at 349.

20/ (continued)

> "it is irrelevant to the remedial purposes of the [Hawaii] Securities Act that an investor participates in a minor way in the operations of the enterprise. Courts should focus on the quality of the [investor's] participation. In order to negate the finding of a security the offeree should have practical and actual control over the managerial decisions of the enterprise." 485 P. 2d at 111.

As discussed at pages 7-9, supra, the purchasers of distributorships or field manager positions participated only in a very limited and "minor way in the operations of the enterprise" and lacked both "practical and actual control over the managerial decisions."

Second, in the release relied upon by appellants, the Commission, although it cited the Hawaii Market Center decision with approval, did not limit itself to the standards adopted therein. Rather, the Commission stated,

> ". . . in the Commission's view a security is offered or sold where the franchisee is not required to make significant efforts in the operation of the franchise in order to obtain the promised return."

Securities Exchange Act Release No. 9387 (November 30, 1971) at 2. This test was properly applied by the court below.

The court below also held that the interests in Galaxy involved investment contracts with respect to Galaxy's proposed retail sales operations, as well as with respect to the sale of additional distributorships and field managers positions (A 1792-96).[21/] While we recognize that this holding goes further than the decisions in Koscot Interplanetary, Inc., supra, and Glenn W. Turner Enterprises, Inc., supra, which only considered interests involving commissions on the sale of investment interests to others, we submit that the lower court was correct.

Purchasers of field manager positions and distributorships made substantial investments in Galaxy and thereby provided its capital. In return, Galaxy did not offer a traditional franchise, allowing franchisees to establish and operate a business, using the Galaxy name and/or receiving certain services from Galaxy. Compare Mr. Steak, Inc. v. River City Steak, Inc., 460 F. 2d 666 (C.A. 10, 1972). If Galaxy's retail operations had developed according to plan, investors in field manager positions would only have to recruit salesmen; those who invested in distributorships would only have to recruit field managers; Galaxy would take care of the rest. It promised to train the salesmen, pay them, and take and fill their customers' phone orders and reorders. In fact, Galaxy represented that, in order

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21/ The lower court analyzed separately both aspects of the Galaxy scheme, that is, the marketing of sales distributorships and its proposed retail sales operations, concluding that each fell within the definition of a security. Cf. Securities and Exchange Commission v. United Benefit Life Insurance Co., 387 U.S. 202, 207 (1967). If this Court affirms the lower court's findings with respect to either aspect of the Galaxy scheme, appellants' jurisdictional challenge must fail.

for an investor to receive a handsome return on his capital, it would not even be necessary for his salesmen to continue to exert efforts, since Galaxy promised to pay commissions on reorders regardless of whether the investor or the salesmen ever contacted the customer again. Here, as in Howey, 328 U.S. at 300,

> "all the elements of a profit-seeking business venture are present . . . . The investors provide the capital and share in earnings and profits; the promoters manage, control and operate the enterprise."

At page 14 of their brief, defendants cite numerous cases in support of their position that a franchise is not a security; however, as defendants themselves acknowledge, the franchises considered in all the cases cited required the franchisee to "perform significant tasks in order to realize benefits." (Ibid.) We do not disagree that a true franchise, where the franchisee operates a business and makes policy determinations, is not an investment contract.

Juristiction over this action could also be upheld on the ground that the interests offered and sold by Galaxy were either "certificates of interest or participation in . . . profit sharing agreements[s]" or other interests "commonly known as a security," within the definition of security. See Section 2(1) of the Securities Act and Section 3(a)(10) of the Exchange Act, quoted in note 15, supra.

In United Housing Foundation v. Forman, supra, 421 U.S. at 852, the Supreme Court stated:

> "The touchstone [of its decisions defining "security"] is the presence of an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others."

In that same opinion, the Supreme Court stated that "profits," in this context, include "participation in earnings resulting from the use of investors funds." (Ibid.) The evidence in the record in this action reveals that purchasers of the field manager positions and distributorships were led to believe that they would receive substantial returns generated by the enterprise which Galaxy's management was to develop and operate, using the capital the purchasers had supplied. Therefore, in a fundamental sense, the interests offered and sold by appellants were "securities."

B. Appellants' Violated and Aided and Abetted Violations of the Antifraud Provisions of the Federal Securities Laws by Knowingly and Recklessly Misrepresenting and Omitting To State Material Facts in Connection with the Offer and Sale of Investments in Galaxy.

Appellants argue (Br. 16-18) that the Supreme Court's recent decision in Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976), requires that the Commission plead and prove that they acted with "scienter" in this action seeking equitable prophylactic relief based, in part, on alleged violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. This argument ignores the finding of the court below that appellants Kirsch and Shevack knowingly or recklessly[22/] misrepresented and omitted to state material facts in connection with the offer and sale of interests in Galaxy (A 1805-09).[23/]

22/ In Hochfelder, supra, 425 U.S. at 194, n.12, the Supreme Court defined scienter as "a mental state embracing intent to deceive, manipulate or defraud." In the same footnote the Supreme Court left "open the question whether, in some circumstances, reckless behavior is sufficient for civil liability under §10(b) and Rule 10b-5," even in a private action.

23/ In this respect, and unlike the allegedly negligent accountants involved in Ernst and Ernst v. Hochfelder, supra, Kirsch's and Shevack's active

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In any event, this Court squarely rejected, in its recent decision in Securities and Exchange Commission v. Universal Major Industries Corp., [Current] CCH Fed. Sec. L. Rep. ¶96,805 (C.A. 2, Dec. 16, 1976), the argument that scienter is necessary to be proved by the Commission in an enforcement action. In Universal Major Industries, this Court reaffirmed its well-established precedents to the effect that negligence, not scienter, is the standard of care in Commission injunctive actions,[24/] stating that

> "[W]e [have] also made it clear that in SEC proceedings seeking equitable relief, a cause of action may be predicated upon negligence alone, and scienter is not required. While this rule has not met with universal approval [citations omitted], it is nonetheless the law of this circuit." Id. at 90,916.

In addition, the United States Court of Appeals for the First Circuit, the only other appellate court to consider this issue since the Supreme Court's decision

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23/ (continued

participation in the Galaxy scheme was similar to the conduct of the defendants in Herzfeld v. Laventhol, Krekstein, Horwath & Horwath, [Current] CCH Fed. Sec. L. Rep. ¶95,660 (C.A. 2, July 15, 1976)--conduct which this Court held satisfied the scienter requirement established by the Supreme Court in Hochfelder for private actions seeking damages under Section 10(b) and Rule 10b-5. As this Court noted in Herzfeld:

> "The [defendants] . . . here are not being cast in damages for negligent nonfeasance or misfeasance, but because of their active participation in the preparation and issuance of false and materially misleading accounting reports on which Herzfeld relied to his damage." Id. at 90,261.

See also United States v. Charnay, [1975-76 Transfer Binder] CCH Fed. Sec. L. Rep. ¶95,560 (May 7, 1976), petition for rehearing en banc denied, July 8, 1976, petition for certiorari denied, December 6, 1976.

24/ See Securities and Exchange Commission v. Management Dynamics, Inc., 515 F. 2d 801 (C.A. 2, 1975); Securities and Exchange Commission v. Spectrum, Ltd., 489 F. 2d 535 (C.A. 2, 1973); and Securities and Exchange Commission v. Texas Gulf Sulphur Co., 401 F. 2d 833 (C.A. 2, 1968), certiorari denied sub nom. Coates v. Securities and Exchange Commission, 394 U.S. 976 (1969).

in Hochfelder, also has held that the Commission is not required to plead and prove scienter in an injunctive action based on violations of the antifraud provisions of the federal securities laws. See Securities and Exchange Commission v. World Radio Mission, [Current] CCH Fed. Sec. L. Rep. ¶95,751 (C.A. 1, Nov. 4, 1976).

Further, the scienter requirement for private actions seeking damages established by the Supreme Court in Hochfelder is based on the specific language of Section 10(b)[25/] and clearly is not applicable to actions brought under either Section 5 or 17(a) of the Securities Act. See Securities and Exchange Commission v. Universal Major Industries, supra, ¶95,804 at 90,196. See also Securities and Exchange Commission v. World Radio Mission, supra, ¶95,751 at 90,661. Thus, the lower court's findings that Kirsch and Shevack aided and abetted violations of Section 5 and violated and aided and abetted violations of Section 17(a) of the Securities Act would alone be sufficient to sustain the equitable prophylactic relief granted, even without the finding that the latter section was knowingly and recklessly violated.

25/ See Hochfelder, supra, 425 U.S. at 192-201. The Supreme Court noted that the broad language of Rule 10b-5(b) and (c), which is virtually identical to the language of Section 17(a) of the Securities Act, could "be read as proscribing . . . any type of material misstatement or omission, and any course of conduct that has the effect of defrauding investors, whether the wrongdoing was intentional or not," but held that the "scope [of Rule 10b-5] cannot exceed the power granted the Commission by Congress under §10(b)." (Id. at 212-214.) Section 17(a) is not a rule, however, but an independent statute.

CONCLUSION

For the foregoing reasons, the order of the district court should be affirmed.

Respectfully submitted,

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January 1977

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

OFFICE OF THE
GENERAL COUNSEL

January 24, 1977

A. Daniel Fusaro
Clerk,
United States Court of
Appeals for the Second Circuit
United States Court House
Foley Square
New York, New York 10007

Re: Securities and Exchange Commission v. Galaxy Foods, et al.,
Docket No. 76-6161

Dear Mr. Fusaro:

Enclosed for filing in the above-referenced appeal are ten copies of the brief of the Securities and Exchange Commission, appellee.

I certify that on this date, January 24, 1977, I also mailed two copies of said brief, postage prepaid, to:

Alan I. Goidel
Goidel, Goidel & Helfenstein, P.C.
127 John Street
New York, New York 10038
Counsel for appellants

If you have any questions regarding this filing, please call either Kathryn B. McGrath at (202) 755-1142 or me at (202) 755-1387.

Sincerely,

Vernon I. Zvoleff

Vernon I. Zvoleff
Attorney

Enclosures